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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

ORIGINAL

Review Of Use Of Appropriated Funds For Defense Commissary Operations

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The Army, the Air Force, and the Marine Corps continue to spend several millions of dollars each year in appropriated funds for certain commissary operating expenses which, by law, should be paid from commissary revenues. Although GAO reported on the improper subsidizing of commissary operations 6 years ago, Defense has not taken corrective action.

GAO recommends that Defense take action to ensure that required costs are borne by commissary patrons.

GAO further recommends that the Secretary of Defense emphasize to the military services the need to comply with existing Defense directives in future funding of commissary operations.

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AUGUST 11, 1982

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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D.C. 20548

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To the President of the Senate and the
Speaker of the House of Representatives

This report addresses the improper subsidization of Department of Defense commissary operations from appropriated funds. We performed this review to determine if Defense was complying with congressional intent regarding the use of these funds. The information is provided for use in considering future Defense appropriation requests.

Copies of this report are being sent to the Director of the Office of Management and Budget and to the Secretary of Defense.

Charles A. Bowsher

Comptroller General
of the United States

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COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

REVIEW OF USE OF APPROPRIATED FUNDS FOR DEFENSE COMMISSARY OPERATIONS

D I G E S T

The Army, the Air Force, and the Marine Corps continue to spend millions of dollars each year in appropriated funds for certain commissary operating expenses which, by law, should be paid from commissary revenues. Although GAO reported on this improper subsidization of commissary operations 6 years ago, Defense has not taken adequate corrective action.

GAO made this review to determine if Defense had taken appropriate action to comply with the intent of the Congress to ensure the proper funding of certain operating expenses. The review was designed to provide the Congress with information to use in considering future Defense appropriation requests.

The commissary program is financed with both appropriated funds and commissary revenues. Funds appropriated by the Congress are used to finance resale inventory and pay personnel costs, but most other expenses are required to be paid from commissary revenues.

The Defense appropriations acts, since 1952, have prohibited the use of appropriated funds for certain expenses of commissaries located in the continental United States, such as the cost of purchase and maintenance of store equipment, supplies, and commissary utilities. The Department of Defense directives issued to implement the appropriations acts also required that commissary revenues be used for these expenses.

In 1975, GAO reported that substantial expenses required to be paid from commissary revenues were paid instead from appropriated funds. The Army Audit Agency issued a similar report on Army operations in 1977. In 1980, GAO issued another report which concluded that commissaries could pay for their costs and thereby decrease their dependence on appropriated funds.

Although Defense acknowledged during the 1976 appropriations hearings that a funding problem

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did exist and advised the Congress that action would be taken to ensure that proper funds were used to pay commissary expenses, this study revealed that the Army, the Air Force, and the Marine Corps continue to subsidize commissary operations with appropriated funds. Defense directives require the use of commissary revenues for certain expenses, but management is not emphasizing these requirements. Only the Navy was found to be in full compliance with the law and Defense directives. The other services did not ensure that commissary revenues were used for appropriate commissary expenses.

OPERATING EXPENSES WERE IMPROPERLY PAID WITH APPROPRIATED FUNDS

During fiscal 1980 alone, the Army, the Air Force, and the Marine Corps together used $3.8 million in appropriated funds for (1) intrabase transportation, (2) purchase and maintenance of equipment, (3) supplies, and (4) utilities. The improper use of appropriated funds for these purposes continues despite Defense's assurances to the Congress during the 1976 hearings that the problem would be corrected. GAO believes the services should use commissary revenues to reimburse appropriated funds for all such expenses incurred since the beginning of fiscal 1976. (See p. 3.)

EQUIPMENT WAS USED IN COMMISSARY OPERATIONS WITHOUT REIMBURSEMENT

The Army, the Air Force, and the Marine Corps provided equipment without charge for use in support of commissary operations. In fiscal 1981, this equipment, including vehicles and office furniture and equipment, had a cost of $3.7 million. Because the commissaries may not have a permanent need for some of this equipment, GAO believes appropriated funds should be reimbursed by an amount equal to either the cost of this equipment or an appropriate rental charge. (See p. 10.)

USE OF APPROPRIATED FUNDS FOR DATA PROCESSING EQUIPMENT WAS UNAUTHORIZED

In fiscal 1977, the Air Force used $3.6 million in appropriated funds for the purchase and maintenance of data processing equipment to be used

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exclusively in its commissary system. This use of appropriated funds was prohibited by law. (See p. 11.)

SERVICES SHOULD COMPLY WITH EXISTING DIRECTIVES

Congressional prohibition against the use of appropriated funds to subsidize certain commissary operating expenses is longstanding. Despite this, such use continues because the military services have adopted widely divergent funding practices that conflict with the intent of the Congress and Defense directives. The Navy and the Marine Corps have generally complied with the law and recovered more of their operating expenses than have the other services. The Navy, in fact, has demonstrated that commissaries can assume a greater share of operating costs and still provide substantial savings to patrons.

RECOMMENDATIONS

GAO recommends that the Secretary of Defense direct the military services to use existing commissary revenues to reimburse appropriated funds for the following:

--Expenses incurred for the cost of intrabase transportation, purchase and maintenance of operating equipment, supplies, and utilities for commissaries, beginning with fiscal 1976.

--The cost of, or a reasonable rental charge for, equipment used primarily to support commissary operations.

--The cost of purchasing and maintaining the data processing equipment purchased by the Air Force in fiscal 1977 for the commissary system.

GAO further recommends that the Secretary of Defense emphasize to the military services the need to comply with existing Defense directives in funding commissary operations in future years.

AGENCY COMMENTS

Defense contends that GAO has not applied the law and the implementing Defense directive properly in making determinations as to which expenses should be reimbursed by the commissaries.

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However, except for costs of intrabase transportation of commissary items, Defense either agreed that the use of appropriated funds was questionable or that it would investigate the propriety of using appropriated funds for the expenses GAO questioned. The reimbursement from commissary revenues for intrabase transportation costs is consistent with the appropriation act provision which requires commissaries to pay costs of operation and maintenance of equipment. Defense should reconsider its position on this item of expense.

Defense should expedite its investigation of the expenditures it agrees are questionable and require that commissary revenues reimburse appropriated funds as indicated in GAO's recommendation.

With regard to GAO's recommendation that the Secretary of Defense emphasize to the military services the need to comply with existing Defense directives, Defense stated that it believes the services are largely in compliance but will take steps to ensure that proper funds are used for commissary operations.

Defense's reply is included as appendix II. A summary of the Defense comments and GAO's evaluation of those comments are on pages 12 to 14.

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CHAPTER 1

INTRODUCTION

The Congress has repeatedly requested the Department of Defense to improve its commissary management and operations. We made this review to determine if Defense was complying with its own directives and the intent of the Congress that commissary revenues be used to pay certain commissary operating expenses, thereby reducing the need for appropriated funds.

In fiscal 1980, the military services operated 358 commissary (supermarket) stores in the United States and abroad. These stores, whose customers are military personnel and other authorized persons, had annual sales of more than $3.6 billion in fiscal 1980 as shown in the following table.

	Continental United States		Overseas		Total	
Service	Number of stores	Annual sales (millions)	Number of stores	Annual sales (millions)	Number of stores	Annual sales (millions)
Army	72	$1,066	70	$241	142	$1,307
Air Force	88	1,322	34	272	122	1,594
Navy	60	544	21	67	81	611
Marine Corps	11	112	2	2	13	114
Total	231	$3,044	127	$582	358	$3,626

FUNDING OF COMMISSARY OPERATIONS

The commissaries are financed both from appropriated funds and from retail sales receipts. The former are used to finance resale inventory and pay personnel costs. The latter are used to replace commissary resale inventories. The markup, or surcharge, on the items sold creates commissary revenues.

Beginning in 1952, 1/ every Defense appropriation act has prohibited the use of appropriated money for certain commissary operating expenses (see app. I). These acts provided that

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1/Sec. 628, Department of Defense Appropriations Act, 1952, Public Law 82-179, 65 Stat. 449.

"* * * No appropriation contained in this Act shall be available * * * in connection with the operation of commissary stores of the agencies of the Department of Defense for the cost of purchase (including commercial transportation in the United States to the place of sale * * *) and maintenance of operating equipment and supplies and for the actual or estimated cost of utilities as may be furnished by the Government * * *."

The hearings associated with the 1952 act revealed the Congress' intention that the Army and the Air Force reflect overhead costs in their commissary prices, including purchase and maintenance of operating equipment, comparable to that included in the prices of Navy commissaries. The Navy commissary regulation, supplied for the record at the 1952 hearings, directed that store prices be established to cover the cost of purchase and maintenance of operating (including office) equipment and supplies. It is a longstanding practice in the Navy to charge such costs (excluding salaries) to commissary revenues.

The operating costs that are required to be funded with commissary revenues are described in Department of Defense Directive 1330.17, dated May 4, 1978. This directive prescribes that commissary revenues collected from store patrons will be used to fund the following:

--Commercial transportation of commissary store merchandise in the United States to the original point of resale.

--Supplies consumed in or provided for the operation of commissary stores.

--Store equipment, including installation and contract cost of commercial or Government maintenance (both preventive maintenance and repair).

--Utilities, including telephone service.

--Acquisition, construction, conversion, expansion, and installation of equipment, or any improvement of commissary store facilities.

When these expenses are paid from appropriated funds, the directive requires reimbursement of these funds from commissary revenues.

To generate the necessary revenues, the Army and the Air Force levy a 4-percent surcharge on sales. The Navy and the Marine Corps use variable product pricing, which generates about a 6-percent markup on sales. The excess revenues accruing from surcharges and merchandise markups are used to pay the operating expenses mentioned above (either directly or as a reimbursement to appropriated and stock funds).

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To comply with the Defense appropriation acts, sales receipts are accounted for separately from surcharge receipts. Sales receipts based on the cost of items sold are deposited as appropriated funds and used to replace commissary resale inventory, while surcharge receipts or markups are deposited in separate trust fund or commissary revenue accounts managed by the military services.

ORGANIZATION OF COMMISSARY OPERATIONS

Each service has an independent system for managing and operating its commissaries. The U.S. Army Troop Support Agency at Fort Lee, Virginia, manages the Army commissary system through four continental U.S. regional offices and one European office. The Air Force Commissary Service at Kelly Air Force Base, Texas, manages and operates Air Force commissaries through 15 continental U.S. offices and two overseas regions. The Navy Resale and Services Support Office at Brooklyn, New York, manages Navy commissaries through 10 continental U.S. and 1 overseas regional/field support offices. The Marine Corps has no single command responsible for the management of commissary stores, but overall policy is provided by Marine Corps Headquarters, Rosslyn, Virginia, and action was recently initiated to centralize commissary management with the establishment of the first of two planned complex offices.

EARLIER AUDIT REPORTS ON THIS SUBJECT

In response to a request from the House Appropriations Committee, we issued a report in 1975 on commissary operations. 1/ One of our findings was that the military services used appropriated funds to pay expenses that were required to be borne by the commissary patrons. The report stated that at 10 commissaries reviewed, appropriated funds totaling $372,800 and $401,800 in fiscal 1973 and 1974, respectively, were used to pay for utilities, supplies, and equipment for warehouses and commissary administrative offices; maintenance on commissary equipment; data processing equipment; local transportation; and laundry services. Such use of funds was in apparent contradiction to the appropriation acts.

This issue was discussed during the fiscal 1976 appropriation hearings. At that time Defense stated it was unable to estimate the dollar value of appropriated funds that may have been used in lieu of commissary revenues to pay commissary expenses. Defense also stated that it had initiated action to ensure proper use of funds to pay commissary expenses and the Air Force had been designated as executive agent for this effort. In an attempt to resolve the funding problems, the Air Force instituted meetings of the four services, but encountered difficulties arising mostly

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1/"Information on Commissary Store Operations" (FPCD-75-132, Mar. 19, 1975).

from major differences in modes of operation. The services failed to achieve full cooperation and agreement, and little has been accomplished since May 1977.

The U.S. Army Audit Agency issued a report to the Army Troop Support Agency in November 1977 which questioned the use of appropriated funds for supplies and equipment in commissaries. The report recommended that:

--Directives be revised to provide for the financing of all commissary equipment and administrative supplies from surcharge funds.

--Installations be advised that costs of purchase, maintenance, and operation of equipment and supplies used for commissary resale operations must be paid from surcharge funds.

--Appropriated funds be reimbursed for the cost of purchase, maintenance, and operation of the commissary equipment provided by installations.

The recommendations were not adopted and no actions were taken.

Because of congressional concern over the growing need for appropriated fund support of commissary operations, we issued a report in 1980 on the management improvements needed. 1/ This report showed that one of the major stumbling blocks to a more efficient and economical commissary operation was the services' retention of four distinct methods of funding commissary operating expenses through varying interpretations of Defense directives and the law. These problems continue.

OBJECTIVES, SCOPE, AND METHODOLOGY

The overall objective of our review was to determine if Defense had taken appropriate action to comply with the law to ensure the proper funding of certain operating expenses. More specifically, the review focused on the use of appropriated funds for these expenses and was designed to provide the Congress with information for use in considering future Defense appropriation requests.

We examined applicable Department of Defense and military service regulations, accounting procedures and reports, computer printouts, and other documents related to funding of commissary operations and discussed this funding with responsible officials. We reviewed the legislative history of restrictions on the use

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1/"Military Commissaries: Justification as Fringe Benefit Needed--Consolidation Can Reduce Dependence on Appropriations" (FPCD-80-1, Jan. 9, 1980).

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of appropriated funds in connection with commissary operations. Since these restrictions were found to have originated with the 1952 Defense Appropriations Act, our legal review concentrated on the legislative history of the act.

To determine Defense policies and procedures for using appropriated funds or surcharge funds for various operating expenses of commissary stores and supporting activities, we visited nine commissary offices. These included all four of the military services' commissary headquarters: the Navy Resale and Services Support Office, Brooklyn, New York; the Air Force Commissary Service, Kelly Air Force Base, Texas; Headquarters, U.S. Army Troop Support Agency, Fort Lee, Virginia; and the Marine Corps Headquarters, Facilities and Services Division, Rosslyn, Virginia. We visited one of the Army's four regional commissary offices: the Southeast Commissary Region, Fort Lee, Virginia; one of the Air Force's 15 complex offices located in the continental United States: the Capital Commissary Complex, Langley Air Force Base, Virginia; one of the Navy's two regional/field support offices located in the continental United States: the Navy Field Support Office, Norfolk, Virginia; and the only Marine Corps complex office: the Marine Corps West Coast Commissary Complex, El Toro Marine Corps Air Station, California. We also discussed funding policies with officials in the Office of the Secretary of Defense.

We obtained information from the Army Troop Support Agency, the Navy Resale and Services Support Office, and the Air Force Commissary Service on the funding and value of installation support provided to commissary stores and support activities. At our request, these three headquarters activities asked each continental U.S. installation having a commissary to give them a valuation of installation services and equipment, machines, and furniture supplied to commissary operations on a nonreimbursable basis during fiscal 1979, 1980, and part of 1981. After reviewing for reasonableness, the headquarters activities provided us this information on appropriated funds used.

The review was made during January through September 1981. Using the procedures described above, we obtained data on commissary operating expenses and the type of funds used to meet these expenses for all stores in the United States for fiscal 1979, 1980, and part of 1981. Complete fiscal 1981 data were not yet available at the conclusion of our review. Because different requirements and authorizations apply to overseas commissaries, we limited our study to continental U.S. commissary stores. These generate about 80 percent of total commissary sales.

Our review was made in accordance with GAO's current "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions," except that the financial information we used in the report is based mainly on Defense accounting records and information provided by Defense officials. The information was evaluated for reasonableness but could not be verified because of the large number of commissaries involved and their wide dispersal.

Also, because our review was conducted at one regional office or commissary complex office in each military service, peculiarities may exist in the use of appropriated and surcharge funds that were not disclosed by our review. However, the four locations we chose operate under standard funding guidelines and use similar accounting and financial management systems.

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CHAPTER 2

APPROPRIATED FUNDS ARE STILL BEING IMPROPERLY USED TO SUBSIDIZE COMMISSARY OPERATIONS

With the notable exception of the Navy, the military services are still spending millions of dollars of appropriated funds each year for commissary operating expenses which, by law, should be paid by commissary patrons. For nearly 30 years, Defense appropriation acts have prohibited the use of appropriated funds for such expenses as the cost of purchase and maintenance of store equipment, supplies, and commissary utilities. Despite these prohibitions, and despite our earlier report in 1975 that the military services were using appropriated funds to pay for operating expenses that should have been paid from commissary revenues, the problem still exists today. Defense acknowledged this problem during the 1976 appropriations hearings, and advised the Congress that in the future it would ensure that proper funds were used to pay commissary expenses. However, our current review disclosed that appropriate action has not been taken and appropriated funds are still subsidizing commissary operations.

The disbursements we found that violated Defense directives and improperly used appropriated funds are as follows:

--$3.9 million was spent by the Army, the Air Force, and the Marine Corps for intrabase transportation, purchase and maintenance of equipment, supplies, and utilities for commissary operations during fiscal 1980 alone.

--$3.7 million was spent for Army, Air Force, and Marine Corps equipment provided without charge from October 1, 1980, through August 30, 1981, and used primarily in support of commissary operations.

--$3.6 million was spent for data processing equipment purchased in fiscal 1977 for Air Force commissaries.

Following are detailed discussions of the aforementioned violations.

APPROPRIATED FUNDS HAVE NOT BEEN REIMBURSED AS REQUIRED BY LAW

Improper use of appropriated funds for commissary operations has continued because congressional and Defense limitations have not been followed. By limiting the types of expenses to be borne by appropriated funds, the Congress wanted to ensure that all services would recover the cost of certain operating expenses from commissary patrons. However, most of the military services have not complied with the legal restrictions.

Public Law 82-179, its successors, and Defense Directive 1330.17 (see app. I) all provide that commissary revenues are to be used to reimburse appropriated funds for certain commissary expenses,

but the military services have not effectively complied with these requirements. Our review showed that the Navy and, in most cases, the Marine Corps did a better job and recovered more of their operating expenses from commissary revenues than did the other services. When the issue was raised during the 1976 appropriation hearings, Defense's representative indicated that action would be initiated to ensure that proper funds were used to pay commissary expenses. However, 6 years later, we found that the military services continue to follow widely divergent funding practices and to improperly use appropriated funds in apparent contradiction of the appropriations acts. These practices resulted in the improper expenditure of appropriated funds without reimbursement for (1) commissary operating expenses, (2) installation equipment to support commissary operations, and (3) data processing equipment for use in commissary stores. Details on these improper expenditures follow.

Operating expenses were improperly paid with appropriated funds

The Army, the Air Force, and the Marine Corps used $3.9 million in appropriated funds to pay for intrabase transportation, operating equipment, supplies, and utilities for commissary operations during fiscal 1980. Using data provided at our request by the military services, we determined that the following costs were improperly absorbed by appropriated funds in fiscal 1980.

Type of expense	Appropriated funds used				
	Army	Air Force	Navy	Marine Corps	Total
	(thousands)				
Intrabase transportation of merchandise (note a)	$ 439	$203	-	$65	$ 707
Office furniture and equipment (includes maintenance)	1,769	196	-	-	1,965
Operating and administrative supplies	476	114	-	-	590
Utilities	490	31	-	-	521
Total	$3,174	$544	-	$65	$3,783

a/In Defense's May 26, 1982, reply to our report it argues that the law does not require that intrabase transportation expenses be reimbursed by commissary surcharges. The expense, for the most part, includes the use of appropriated fund equipment such as trucks and forklifts to move merchandise from the warehouse to the commissary stores. We believe the law does require such expenses to be reimbursed. A further discussion of the matter is on p. 13.

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The inconsistencies in the use of commissary revenues reflect the wide divergence that exists among the commissary funding policies of the four services. The following table allows comparison of these policies.

Are all expenses paid from commissary revenues?

Type of expense	Army	Air Force	Navy	Marine Corps
Intrabase transportation of merchandise	No	No	Yes	No
Office furniture and equipment:				
Commissary stores	No	Yes	Yes	Yes
Commissary administrative activities	No	No	Yes	Yes
Administrative supplies:				
Commissary stores	No	Yes	Yes	Yes
Commissary administrative activities	No	No	Yes	Yes
Utilities:				
Commissary stores	Yes	Yes	Yes	Yes
Commissary administrative activities	No	No	Yes	Yes

As shown, the Army and the Air Force rely on appropriated funds to support store operations, while the Navy and the Marine Corps rely almost entirely on commissary revenues. Our review of the 1952 appropriations hearings (see p. 2) indicates that the Congress intended that the Army and the Air Force reflect overhead costs in their commissary prices comparable to those included in the prices of Navy commissaries. It is a longstanding practice in the Navy to charge such costs (excluding personnel costs) to commissary revenues.

Of the $3.8 million in appropriated funds improperly used, most of the Army and Air Force and all of the Marine Corps expenditures occurred because host installations were not reimbursed from commissary revenues for the supplies and services they provided. However, the Army and the Air Force also directly used appropriated funds for the purchase of administrative supplies and office furniture and equipment, and for equipment maintenance.

The Army's position on funding commissary operations has been that administrative equipment and supplies are not required to be purchased from commissary revenues. The Army Troop Support Agency, which manages the Army commissary system, stated in reply to the Army Audit Agency's 1977 report (see p. 4) that the Army was not required to reimburse appropriated funds for these expenditures. This position differs from that of the other services and conflicts with the appropriation acts and Defense directives.

The Air Force differed from the Army in that it funded all equipment and supplies used within the confines of the commissary store with commissary revenues, but not equipment and supplies purchased for commissary management activities physically located outside the store. These activities exist to manage and support the commissaries. We believe the function performed, rather than the location of the function, should determine the funds to be used.

Also, the Air Force expects to use substantially larger amounts of appropriated funds for these commissary management activities in the future. More management activities are being relocated outside the commissary stores and the Air Force expects to use appropriated funds to pay the operating expenses (primarily equipment and supplies) of these activities. In fiscal 1980, the Air Force spent $182,000 for these management activities; in the first 9 months of fiscal 1981, it spent $265,000 for them.

Although the legislation and Defense Directive 1330.17 both require that these operating expenses be paid from commissary revenues, only the Navy has fully complied. Defense officials were fully aware of the restrictions at the time of the 1976 appropriation hearings and advised the Congress that they had initiated action to ensure that proper funds would be used to pay commissary operating expenses. The Air Force was designated as executive agent for this effort but little has been accomplished since 1977. As a result, action has not been taken to comply with the law. We believe the military services should use available commissary revenues to fully reimburse appropriated funds for operating expenses incurred for intrabase transportation, operating equipment, supplies, and utilities since the beginning of fiscal 1976.

Defense equipment was used in commissary operations without reimbursement

In addition to providing installation support services to the commissary operations without reimbursement, the Army, the Air Force, and the Marine Corps also allowed the commissaries free use of equipment that was purchased with appropriated funds. We found no evidence that the Navy was doing this.

According to the Army Troop Support Agency, in September 1981 the Army commissaries and regional offices had on hand about $1.9 million worth of appropriated fund equipment, such as cars, trucks, and office equipment, provided by host installations. The Air Force Commissary Service headquarters estimated in July 1981 that Air Force commissaries and commissary management activities had on hand about $1.7 million worth of appropriated fund equipment provided by host installations. The Marine Corps Headquarters commissary activity reported that Marine Corps stores had on hand appropriated fund equipment costing about $105,000.

We recognize that the commissaries may not have a permanent need for all the appropriated fund equipment they have on hand.

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Thus, in some instances, it may not be feasible for the commissaries to procure this equipment. When equipment is on temporary loan to a commissary, commissary revenues should be used to reimburse the appropriated funds for a reasonable rental charge based on all costs attributable to use of the equipment by the commissary.

Appropriated funds were used for data processing equipment without authorization

In 1977, the Department of the Air Force authorized about $3.6 million of appropriated funds for the acquisition, installation, and operation of data processing equipment to improve the commissary control functions. Of this amount, $2.7 million was funded by a one-time program for capital investment. An additional $923,000 of appropriated funds was spent on maintenance contracts for this equipment. This use of appropriated funds was not consistent with the requirements of the Defense Appropriations Act. The Air Force justified the procurement as needed "to automate selected control section functions" in the commissaries. Nothing in the justification indicates that the equipment was intended for other than exclusive commissary use. The Air Force explained that the equipment, by permitting automation of processes then performed manually, ultimately would reduce manpower needs. Since the positions to be affected were funded with appropriated funds, the Air Force concluded that the equipment replacing those positions also could be paid for out of appropriated funds.

The Air Force's conclusion was incorrect. We found that the projected savings were not realized because the personnel positions, rather than being eliminated, were redistributed within the commissary system. Even if savings had been achieved, however, the equipment would not have lost its character as equipment used exclusively and directly for commissary operations, which may not be paid for with appropriated funds. The replacement of employees would not except the purchase from the express prohibition against use of appropriations for purchase of operating equipment. Accordingly, the Air Force should have used surcharge funds for the purchase and maintenance of the data processing equipment. See appendix I for additional discussion.

CONCLUSIONS

Our 1975 report pointed out that the military services used appropriated funds to pay expenses that were required to be borne by the commissary patrons. During the fiscal 1976 Department of Defense appropriations hearings, Defense stated it had initiated actions to ensure proper funding of commissary expenses. However, Defense still has not taken appropriate action to ensure that proper funds are used to pay certain commissary operating expenses, as required by law. Consequently, the Army, the Air Force, and to a lesser extent the Marine Corps are using appropriated funds, rather than commissary revenues, to pay such expenses. Further, no two military services finance commissary operations identically.

A greater share of the costs of commissary operations should be borne by patrons as required by law and by Defense directives. Our review indicates that the Navy is the only service that has demonstrated compliance with this requirement. In the 1952 appropriations hearings, the Congress indicated its intent that the Army and the Air Force reflect overhead costs in their commissary prices, including purchase and maintenance of operating equipment, comparable to those included in the prices of Navy commissaries. It is a longstanding practice in the Navy to charge such costs (excluding personnel costs) to commissary revenues.

RECOMMENDATIONS

We recommend that the Secretary of Defense direct the military services to use existing commissary revenues to reimburse appropriated funds for the following:

--Expenses incurred for the cost of intrabase transportation, purchase and maintenance of operating equipment, supplies, and utilities for commissaries, beginning with fiscal 1976.

--The cost of, or a reasonable rental charge for, equipment used primarily to support commissary operations.

--The cost of purchasing and maintaining the data processing equipment purchased by the Air Force in fiscal 1977 for the commissary system.

We further recommend that the Secretary of Defense emphasize to the military services the need to comply with existing Defense directives in funding commissary operations in future years.

AGENCY COMMENTS AND OUR EVALUATION

In its May 26, 1982, response to our draft report (see app. II), Defense advised us that it agreed that the military departments should comply with the provisions of the Appropriations Act and the implementing Defense directive to ensure proper funding of commissary store operations. However, with regard to our first recommendation, Defense believes we are not applying the act and Defense directive properly in asserting that the cited expenses were improperly funded by appropriated funds. It is Defense policy that costs of common services, which serve both the commissary stores and other departmental activities, should not be paid from commissary revenues. Defense argues that many of the expenses we questioned are common services' expenses. Defense erred in suggesting that we did not apply the law and directive properly. As Defense knows, in requesting information from the military services during our audit, we specifically asked that costs of common services be excluded and the commissary headquarters verified that the information given to us was correct.

Notwithstanding Defense's main objection, the only expenses it specifically questions without any qualification are those relating

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to intrabase transportation of commissary items. With regard to other expenses discussed in the reply, Defense either agreed that the use of appropriated funds was questionable or saw a need to investigate whether the use of appropriated funds was correct. For example, Defense said that it plans to look into the circumstances surrounding the use of the data processing equipment purchased by the Air Force with appropriated funds.

With regard to expenses relating to intrabase transportation of commissary merchandise, Defense argues that the general provisions of the Appropriations Act indicate that the transportation expenses required to be reimbursed are those for the "cost of purchase" of operating equipment and supplies "including commercial transportation" of such equipment and supplies. Defense says that since intrabase transportation does not fall under any of these categories, commissary revenues should not reimburse such expenses. As shown on page 8 of our report, over $700,000 in appropriated funds was used in fiscal 1980 for intrabase transportation of commissary merchandise. This large expenditure indicates a substantial use of vehicles for which commissaries should at least pay a rental charge. The reimbursement from commissary revenues for intrabase transportation costs is consistent with the appropriation act provision. The statute requires commissaries to pay the costs of operation and maintenance of equipment. In our view, military vehicles used for intrabase transportation are no different than other military equipment provided on a part-time basis for commissary use for which we recommend reimbursement from commissary revenues. Also, given that the intent behind the statute was to require that commissary revenues be used to cover overhead or administrative costs, and that the only specific exclusion in the statute is for overseas transportation, it is reasonable to read the statute as making no distinction between intrabase transportation provided by military vehicles, and other overhead costs provided in kind by the military services. We believe, therefore, that Defense should reconsider its position on the proper funding of this item of expense.

Defense should also expedite its investigation of all of the expenditures we questioned and require that the commissary revenues reimburse appropriated funds for such expenditures as indicated in our recommendation.

With regard to our second recommendation, that the Secretary of Defense emphasize to the military services the need to comply with existing Defense directives, Defense stated that it believes the services are largely in compliance but it will take steps to ensure that appropriated funds support for commissary store operations is proper.

In addition to commenting on our recommendations, Defense objected to our disclosure in the draft report that a large amount of unobligated commissary revenues are available to reimburse appropriated funds for commissary operating expenses that were

previously paid improperly. Defense argues that even if commissary revenues were not sufficient to pay for costs required by law, such costs would have to be paid for from commissary revenues. We agree that the amount of unobligated revenues is not germane to the issue at hand and have deleted references to these revenues in this final report.

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LEGAL OPINION ON THE STATUTORY LIMITATION ON USE OF APPROPRIATIONS FOR MILITARY COMMISSARY OPERATIONS

Based on analysis of the statutory limitation on use of appropriated funds for operation and maintenance expenses of commissaries, we concluded that the law prohibits use of appropriated funds to purchase and maintain equipment to be used solely in commissary operations, even though the equipment was intended to replace personnel who were properly paid from appropriations. A detailed analysis appears below.

QUESTION: Was it proper for the Air Force to use appropriated funds for the purchase and maintenance of data processing equipment for use exclusively in its commissary system?

ANSWER: No.

The provision restricting use of appropriated funds in connection with commissary operations first appeared as section 628 of the Department of Defense Appropriations Act, 1952, Public Law 82-179, 65 Stat. 449, which provides:

> "No appropriation contained in this Act shall be available on and after January 1, 1952, in connection with the operation of commissary stores of the agencies of the Department of Defense for the cost of purchase (including commercial transportation in the United States to the place of sale but excluding all transportation outside the United States) and maintenance of operating equipment and supplies and for the actual or estimated cost of utilities as may be furnished by the Government and of shrinkage, spoilage, and pilferage of merchandise under the control of such commissary stores, except as authorized under regulations promulgated by the Secretaries of the military departments concerned, with the approval of the Secretary of Defense, which regulations shall provide for reimbursement therefor to the appropriations concerned and, notwithstanding any other provision of law, shall provide for the adjustment of the sales prices in such commissary stores to the extent necessary to make such reimbursement: Provided, however, that under such regulations as may be issued pursuant to this section all utilities may be furnished without cost to the commissary stores outside the continental United States and in Alaska." (Emphasis added.)

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That language has been included in every Defense appropriation act since 1952. 1/

The original House bill prohibited use of appropriated funds "for any direct expense * * * in connection with the maintenance, conduct, operation or management" of commissary stores. The House report states that the purpose of the section was to require commissary sales prices to include all the direct costs of commissary operations, except overseas transportation. (H. Rept. 790, 82d Cong., 1st sess. 147 (1951))

The language of the Senate version was more limited, listing particular commissary expenses for which appropriated funds could not be used. Specifically, the Senate version, as described in the Senate report, required that overhead costs, including purchase and maintenance of operating equipment and supplies, be reflected in commissary prices. (S. Rept. 730, 82d Cong. 1st sess. 7 (1951)) The purpose of the section was said to be to require that all the services adopt the Navy's method of funding all its commissary operations out of surcharge revenues. However, unlike the House version, the Senate language did not cover "any direct expense" of commissary operations.

The Senate version, with minor modification, was adopted as the final version in the 1952 act. The conference report, consistent with the House and Senate reports, states that the section provides for adjustment of sales prices to cover "overhead or administrative costs." (H. Rept. 1097, 82d Cong., 1st sess. 9 (1951))

Defense Directive 1330.17 (May 4, 1978) implements the statutory limiting provision. Section IV lists various costs that must be paid for out of surcharge funds. Specifically, section 4-403.3 provides:

> "Commissary store equipment, to include installation, and contract cost of commercial or Government maintenance (includes preventive maintenance and repair), will be paid by direct citation of or reimbursed from funds collected from commissary store patrons."

The data processing equipment or "programmable work stations" purchased by the Air Force appear to fall squarely within the scope of the statute and section 4-403.3 of the directive. Procurement of the work stations and associated software was justified as

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1/Sec. 624 of the 1954 Defense Appropriations Act, Public Law 83-179, 67 Stat. 353, retained the language of the 1952 act but expanded the provision to prohibit use of appropriated funds for military commissaries in areas where adequate commercial facilities are available. See S. Rept. 601, 83d Cong., 1st sess. 8 (1953). That prohibition also has been reenacted each year since 1954.

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needed "to automate selected control section functions" in the commissaries. Nothing in the justification gives a basis for concluding that the work stations were intended for other than exclusive commissary use. Further, this equipment is used exclusively for commissary operations, principally to process purchasing data. Therefore, the work stations constitute equipment used in connection with the operation of commissary stores, within the meaning of the statute.

The Air Force, however, authorized the use of approximately $3.6 million in appropriated funds for the purchase and maintenance of the work stations. The Air Force justified its decision on the grounds that the work stations, by permitting automation of processes then performed manually, ultimately would eliminate 174 manpower spaces. Since those positions were funded with appropriated funds, the Air Force concluded that the equipment replacing those positions also could be paid for out of appropriated funds.

The Air Force's conclusion was incorrect and the projected savings did not occur. Although manpower needs were reduced, the personnel positions were redistributed within the commissary system, not eliminated. Even if savings had been realized, however, the work stations would not lose their character as equipment used exclusively and directly for commissary operations, which may not be paid for with appropriated funds. The fact that the work stations were intended to replace employees who, under the statute, were properly paid from appropriations does not except the purchase from the express prohibition against use of appropriations for purchase of operating equipment. Accordingly, the Air Force should have used surcharge funds for the purchase and maintenance of the work stations.

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ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D.C. 20301

MANPOWER, RESERVE AFFAIRS AND LOGISTICS

26 MAY 1982

Mr. W. D. Campbell
Acting Director, Accounting and
Financial Management Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Campbell:

This is in response to your letter of April 20, 1982, to the Secretary of Defense concerning your draft report "Commissaries Are Still Being Improperly Subsidized by Defense" (AFMD-82-45, OSD Case #5953).

The Department of Defense fully supports the underlying premise of the report that the Military Departments should fully comply with the provisions of the Appropriation Act concerning the operation of commissary stores and the provisions of DoD Directive 1330.17, "Armed Services Commissary Store Regulations," which we believe properly implements the General Provisions concerning commissaries of the Department of Defense Appropriation Act. The Department also believes that the provisions of DoD Directive 1330.17 accurately reflect the intent of Congress concerning the general provision in view of the fact that its provisions have been approved by the Committee on Armed Services of the House of Representatives which has Congressional oversight for commissary operations and, with respect to commissary store appropriated fund support, by the congressional appropriation and authorization process during which appropriated fund support for commissaries is approved by Congress. Given this background, we believe that most of the report's recommendations are based upon a different interpretation of the applicable provisions of the regulation and the general provision as they relate to the facts surrounding the appropriated fund support provided by the Military Departments to their commissary store operations, rather than a different interpretation of the legal requirements applicable to the operation of commissary stores by the Department of Defense.

The report makes two recommendations to the Secretary of Defense. These are:

1. That the Military Departments be directed to use existing commissary revenues to reimburse appropriated funds for:

- Expenses incurred for transportation of items for resale, purchase and maintenance of operating equipment, supplies, and utilities for commissaries beginning with fiscal year 1976.

- The cost of, or a reasonable rental charge for, equipment used primarily to support commissary operations.

- The cost of purchasing and maintaining certain data processing equipment purchased by the Air Force in fiscal year 1977 for the commissary system.

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2. That the Secretary of Defense emphasize to the Military Departments the need to comply with existir Defense Directives in funding commissary operations in future years.

These recommendations are based upon the review of aspects of appropriated fund support provided by the Military Departments during which the General Accounting Office concluded that operating expenses were improperly paid with appropriated funds with respect to the supplying of intrabase transportation of commissary merchandise and the furnishing to commissary stores of office equipment, including maintenance; operating and administrative supplies; and utilities. In reaching this conclusion the report notes that there is a disparity among the Military Departments concerning what should, and what should not, be paid from appropriated funds and surcharge funds and implies that this divergence is the result of a failure on the part of the Army, Air Force, and Marine Corps to follow Department of Defense and Congressional guidance concerning appropriated fund support for commissaries. As will be noted in the enclosure, the Department agrees that some of the items which have been paid for from appropriated funds appear to be items which should have been paid from surcharge funds. We are directing the Military Department concerned to review such expenditures; however, we do not concur with all of the recommendations nor with the conclusion that because there are differences in reimbursement requirements that such differences necessarily reflect a failure to comply with the law or regulations governing commissary store operations. With respect to the matter of the Air Force data processing equipment, the report's conclusion concerning appropriated fund support is based upon the premise that the equipment is used exclusively in commissary store operations; that the use of appropriated funds was premised upon the assumption that it was appropriate to use such funds because personnel spaces paid from appropriated funds would be eliminated; and on the fact that the equipment was not used to perform functions other than those related to commissary store operations. We do not agree that the actual usage of the equipment supports the report's conclusion that the equipment is for the exclusive use of the commissary stores, although we do not have sufficient information at this time to ascertain whether the level of support provided by the equipment permits the usage of such equipment using appropriated funds on the basis that it is common support equipment within the meaning of DoD Directive 1330.17. We will be looking into this matter further with the Air Force.

Finally, with respect to the recommendation that the Secretary of Defense emphasize compliance with law and regulation concerning commissary store operations, we believe that the Military Departments are largely in compliance with the law and regulation governing commissary store operations. We will take corrective action where warranted to ensure that policy of the Military Departments is changed in those few instances where appropriated fund support for commissary store operations conflicts with applicable law and regulation.

We appreciate the opportunity to comment on the draft report. Our detailed comments on the report are attached.

Sincerely,

James N. Juliana

James N. Juliana
Principal Deputy Assistant Secretary of Defense
(Manpower, Reserve Affairs & Logistics)

Enclosure

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DETAILED DEPARTMENT OF DEFENSE COMMENTS ON GENERAL ACCOUNTING OFFICE REPORT "COMMISSARIES ARE STILL BEING IMPROPERLY SUBSIDIZED BY DEFENSE" (Code 903025; OSD Case #5953)

The statutory restrictions concerning the operation of commissary stores are contained in an annual recurring general provision of the Department of Defense Appropriation Act. This provision which appears as section 714 of the Appropriation Act for 1982 (enclosure 2) has been implemented in part 4 of DoD Directive 1330.17, "Armed Services Commissary Store Regulations" (Enclosure 2).

As can be seen from a review of both of these provisions, they require that either direct payment or reimbursement to appropriations be made for the cost of purchase of supplies, including commercial transportation in the United States to the place of resale or use of commissary store merchandise, the purchase and maintenance of operating equipment and supplies; the actual or estimated cost of utilities furnished by the Government; and of shrinkage, spoilage, and pilferage of merchandise under the control of commissary stores. As can also be seen from a review of these provisions, they are specific as to what expenditures are required to be paid for from commissary funds. Although not stated in the general provisions of the Appropriation Act, the general policy of the Department is that commissary stores will be operated with appropriated funds, unless otherwise required by law. This policy is stated in paragraph 4-401 of DoD Directive 1330.17 and reflects the intent of Congress which was stated forcefully in connection with the fiscal years 1976 and 1977 proposals to eliminate appropriated fund support for commissaries. Therefore, with the exception of those items specifically required to be paid for from surcharge revenues, as a general proposition, it is proper to use appropriated funds in support of commissary store operations.

Although it is proper to use appropriated funds to support commissary store operations, this does not mean that all of the Military Departments must use appropriated funds to support aspects of commissary store operations which do not necessarily require reimbursement from commissary store surcharge funds. For this reason, the Department does not ascribe the same significance as does the GAO report to the differences in departmental regulations reflected in the charge on page 9 of the draft report concerning surcharge reimbursements to appropriated funds nor do we believe that such differences reflect that the Military Departments are not in compliance with the law and applicable DoD regulations with respect to all of the categories of expenditures cited on page 9. We do agree, however, that the Army's failure to require reimbursements for office furniture and equipment and administrative supplies used in commissary stores appears to contravene the requirement for reimbursement for the cost of purchase and maintenance of operating equipment and supplies. Accordingly, we will require the Department of the Army to reexamine its policy in these two areas and to make appropriate changes to its regulations governing commissary store operations so that these expenses will be recovered in the future.

With respect to the other aspects of expenditures cited in the report on page 9, we do not believe that the differences among the Military Departments necessarily reflect a failure to comply with law or regulation. To place this issue in context it is necessary to understand the distinction which the Department perceives between the operation of commissary stores, which is addressed in the annual recurring provisions of the Department of Defense Appropriation Act and the commissary programs of the Department of Defense. While we agree that Departmental programs related to the operation of commissary stores themselves should be paid from commissary revenues if those programs are directly and exclusively related to the

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actual day-to-day functioning of the commissary stores, we do not believe that all aspects of administrative activities of commissary store operations should be paid from commissary store revenues. As reflected in paragraph 4-404.2 of DoD Directive 1330.17, common services which serve both the commissary stores and other departmental activities should not be paid for from commissary revenues. For such joint use activities, we believe that it is not proper to require reimbursement to appropriated funds for that portion of the activity which may be used to support or to administer commissary stores. For instance, we do not believe that accounting and other administrative expenses associated with stock fund operations in support of commissary stores or commissary store management activities of the kind discussed on page 3 of the GAO report should be funded from commissary store revenues because they serve legitimate management functions associated with the operation of the Military Departments and they further the obligation of the Military Departments to provide commissary store services to their personnel as much as they further the operation of commissary stores themselves. We believe that it is proper, therefore, to use appropriated funds to support such commissary administrative activities. Not only is such a conclusion supported by the language of the annual general provision in the Department of Defense Appropriation Act but also such a conclusion is supported by the fact that Congress annually appropriates funds for such expenses knowing that such funds will not be reimbursed.

Notwithstanding the conclusion of the foregoing paragraph, we agree with the implication contained in the General Accounting Office report that it would not be possible to avoid the requirement to use commissary store revenues to reimburse appropriated funds merely by moving an activity out of a commissary store physically and relocating it in another area. We believe, as does the GAO, that the proper test to be applied in all cases is the function being performed, not the physical location of that function. Similarly, however, the foregoing conclusion does not necessarily mean that just because a function may currently be located in a commissary store that commissary store revenues should be used to pay for such a function if the function falls within one of the legitimate administrative activities paid from appropriated funds. Thus, while it certainly would appear that the Air Force proposals discussed on pages 9 and 10 of the report to relocate commissary store operation activities outside of commissary building confines would contravene the requirement for commissary store revenue reimbursements, there may be valid reasons why these activities should be paid for exclusively from appropriated funds. Accordingly, we will require the Air Force to carefully examine its expenditures for commissary store related activities to ensure that physical location of those activities is not the only criterion being used to determine whether or not it is appropriate to use appropriated funds, rather than commissary store revenues, to support such activities. We would expect both the Air Force and the General Accounting Office to apply the "function" test rather than the "location" test in determining whether it is proper to use appropriated fund support for the activities summarized on pages 9 and 10 of the GAO report. In this regard, because the GAO report does not identify the functions being performed by the management activities discussed in the report but relies primarily upon the fact that these activities are being relocated, we are unable to state at this time whether or not such activities should be paid for from commissary store revenues or whether such activities should be funded from appropriated funds.

To summarize, we do not believe that it is required for the commissaries to use their revenues to pay for office furniture, equipment, and administrative supplies or utilities in connection with commissary administrative activities if such functions are not directly and exclusively related to the operation of commissary stores themselves. We regard the fact that the Navy requires such reimbursement for such expenses as a difference in policy rather than a difference in applying legal and departmental policy requirements.

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With respect to the intrabase transportation of merchandise cited on page 9 of the GAO report, we also believe that it is proper for appropriated funds to be used to provide such transportation. The General Provisions of the Appropriation Act indicates that the transportation expenses required to be reimbursed are those for the "cost of purchase" of operating equipment and supplies "including commercial transportation" of such equipment and supplies. Not only is intrabase transportation of merchandise not a "cost of purchase" of such merchandise, but also, in most cases, such transportation would not be "commercial transportation" but would be provided by vehicles under the control of the Military Departments and paid for from appropriated funds. We do not consider such use of funds to fall within the definition of transportation of supplies to the place of sale during commercial transportation which is covered by the General Provision in the Appropriation Act.

Insofar as the use of equipment, supplies, and vehicles as described on page 10 of the GAO report, we agree that if such equipment is used exclusively by the commissary stores in their operations, then such equipment should either be purchased using commissary surcharge funds or, if such equipment is not permanently needed, but is used by the commissary stores on a more or less long-term, exclusive basis, then the commissary store surcharge funds should pay a reasonable rental charge based on the cost attributable to usage by the commissary stores. However, we would expect that such a rental charge would not be applied to equipment used on a shared, common basis by the commissaries and other Military Department activities funded with appropriated funds which would fall within the definition of common service items, nor would we expect to charge rent for items borrowed from appropriated fund activities for relatively short periods of time and which are normally used to support departmental activities supported by appropriated funds.

Finally, we would like to address the statements contained in the report concerning the ability of commissary revenues to absorb more costs. While we understand that this portion of the report may have been inserted for any number of reasons, we do not believe that such a consideration is relevant to the basic issues addressed in the report, namely, whether appropriated funds are being used improperly and whether commissary surcharge funds are being used to reimburse appropriated funds for all costs requiring reimbursement by law and by regulations of the Department of Defense. Even if commissary revenues were not sufficient to pay for costs required by law, such costs would have to be paid for from commissary revenues. As we have made it clear, we are in absolute agreement with the premise that those expenditures required to be reimbursed should be paid from surcharge funds. Similarly, however, we strongly object to any inference that, just because there is an apparent availability of commissary revenues, such revenues should be used to fund items of expenditure properly paid for from appropriated funds. Not only would this be contrary to Congressional intent as stated in 1976 and 1977 when the Department of Defense proposed elimination of some aspects of appropriated fund commissary support but also it would be contrary to the express provisions of the General Provision of the Appropriation Act concerning such expenditures and the requirement for reimbursement for some of them.

An unobligated trust fund balance at a particular time is also an unreliable indicator upon which to base a conclusion that commissary revenues can, or should, absorb more costs. There are many other factors to be considered concerning the use of such revenues. For instance, in the Army, there was approximately $30 million in surcharge trust fund open commitments or fund reservations of the $33.1 million cited as available as of June 30, 1981. By September 30, 1981, the uncommitted trust fund balance was $7.8 million which was being held in reserve for a commissary store equipment purchase. Similar situations existed for each of the other Services.

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Surcharge revenues are earmarked for commissary store operating expenses and capital investment. The latter category requires considerable leadtime between initiation of capital investment programs and the actual obligation or expenditure of funds. There are a number of significant commissary store capital investments being planned in all of the Services which will require funding with surcharge trust funds. These investments should increase productivity and result in more effective utilization of the limited manpower available which is supported by appropriated funds. To suggest, however, that appropriately required and proper appropriated fund support should be reduced or that surcharge revenues should absorb more costs is totally unwarranted. Such a suggestion would ultimately require an increase in surcharge charges to the commissary store patrons which we consider to be an unacceptable increased financial burden to military personnel and their families. In addition, such increases would be inconsistent with the desires of Congress and applicable statutory and regulatory provisions concerning appropriated fund support for commissaries.

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